

Midterm 1 Practice

Consider a student with the following monthly nominal expenditure and monthly nominal income:

Year	Soda		Pizza		Nominal Income
	q	p	q	p	
2013	30	\$1.00	30	\$4.00	\$200
2014	30	\$1.10	30	\$4.50	\$200
2015	30	\$1.15	30	\$5.00	\$200

a) Pick a base year and identify what is in the CPI basket

Base year:

CPI basket:

b) Find the price level in each year:

201:

2014:

2015:

c) Find the inflation rate in 2014 and 2015:

2014:

2015:

d) Find the real income in each year:

2013:	2014:	2015:
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e) What is the student's real income growth rate in 2014 and 2015:

2014:	2015:
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f) At the end of 2015 the student got a job with a starting salary of \$2,000 per month (nominal). His employment contract says that each year he will get a 5% increase from the previous year salary. What will his salary be in 2025?

2025:

- g) The student knows that the price level in 2015 is 110. He is pessimistic about inflation and thinks that by 2025 the price level will be 180. Based on this prediction, is his employment contract good? Show how you came up with the conclusion.

Answer:

- h) Statistics say that out of 1000 people in U.S. (including the above student) who graduated in 2015 with the major in Medieval Flemish literature, 300 graduates did not try to look for jobs, and that the unemployment rate for Medieval Flemish literature majors is currently 20%.

Based on these statistics, how many 2015 graduates who majored in Medieval Flemish literature are currently employed?

Answer: